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# "Natural Resources Projects and Native Peoples' Development in the Northwest Territories"

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Summary of Evidence of

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before the

MACKENZIE VALLEY PIPELINE INQUIRY
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# INTRODUCTION

In its recent Discussion Paper on Northern Development the Science Council of Canada posed the following fundamental question: In whose economic interest should the North be developed? (1)

The problems faced by the native peoples of the North indicate an immediate answer to this question: Any development that occurs should first of all benefit the native peoples by contributing in a significant way to their development efforts.

Because the development objectives of the native peoples are of a long-term nature, the most important way in which natural resources projects can contribute to these objectives is related to the economic rents associated with their activities. As the southern provinces of Canada and an increasing number of the less developed countries have come to realize during the last few years, the major long-term benefits that flow from natural resources projects have to do with the appropriation and subsequent utilization of these economic rents. Who receives these rents, and the uses to which they are put, are therefore important areas of study.

A major point at issue in the case of the proposed MacKenzie Valley natural gas pipline is the extent to which the native peoples of the Northwest Territories would benefit from its construction and operation. Since the proposed pipline would presumably operate, in the absence of a negotiated land settlement, under institutional arrangements similar to those that have governed previous natural resources projects, a consideration of the distribution of the economic rents associated with their activities is in order. An analysis of this kind will allow us to see to whom the existing institutional arrangements have directed the long-

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term benefits associated with past natural resources projects in the Northwest Territories, and hence to whom they are most likely to direct those relating to future projects.

In this submission natural resources projects operative in the Northwest Territories since 1970 will be examined from this perspective. Estimates of the magnitude and distribution of the economic rents associated with their activities will be presented, explanations for the observed structures of rent distribution will be advanced, and the implications of this evidence for the relationship between natural resources projects and native peoples' development in the Northwest Territories will be discussed.

## PRELIMINARIES

The estimating procedures utilized to derive the rent and rent distribution estimates presented here may be found in the research studies accompanying this submission. In general, an operating company was not considered as being a rent recipient unless or until it had received a 15 per cent return on its invested capital after taxes.

Rent and rent distribution estimates relate to the years 1970-1974 inclusive. They are expressed in 1975 dollars, and have been converted to 1975 present values by compounding at 10 per cent.

## THE EVIDENCE

### Natural Gas Production at Pointed Mountain

Pointed Mountain is the only producing gas field in the Northwest Territories. Production commenced in August, 1972, and is

conducted by Amoco Canada Petroleum Company Ltd., a wholly-owned subsidiary of Standard Oil Company (Indiana).

An analysis of the rents associated with the Pointed Mountain project between the commencement of production and the end of 1974 revealed the following:

1. The present value in 1975 of these past rents amounted to $66.3 million.

2. Of this total, U.S. producers and/or consumers received $50.7 million, or 76.5 per cent, Canadian entities in British Columbia received $15 million, or 22.7 per cent, and the federal government received $0.6 million, or 0.8 per cent, from royalties.

The reasons for this rather disconcerting structure of rent distribution relate to both the sales arrangements respecting Pointed Mountain natural gas, and to federal government export pricing policy. With respect to the sales arrangements, the contract between Amoco and Westcoast Transmission specified an initial price of 11.5¢ per thousand cubic feet of Pointed Mountain gas. Although the border export price of Canadian gas increased between August, 1972 and December, 1974 from 32¢ to $1 per thousand cubic feet, the price received by Amoco appears to have remained at 11.5¢. This means that entities in British Columbia (with the main candidates being Westcoast Transmission and the provincial government) were receiving a share of the rents associated with Pointed Mountain gas production.

At the same time, the contract under which Westcoast Transmission sold Pointed Mountain gas to its U.S. customer grossly undervalued this gas in terms of its competitive energy value vis-a-vis alternative fuels. In August, 1972, for example, the competitive

energy value of Canadian gas at the U.S. border was around 58¢ per thousand cubic feet, while the actual border price was 32¢. By December, 1974 the actual border price had increased to $1. However, a National Energy Board study published the previous July had indicated that the competitive energy value of Canadian gas exported at Huntington, British Columbia (the export point for Pointed Mountain gas) was $1.57 by March of that year [27].

It was this combination of institutional arrangements that resulted in over 75 per cent of the economic rents associated with the Pointed Mountain project accruing to U.S. residents, while most of the remainder accrued to Canadian entities in British Columbia.

Crude Oil Production at Norman Wells

Production of crude oil at Norman Wells dates from 1921, and is conducted by Imperial Oil Ltd., 69 per cent owned and controlled by the Exxon Corporation, formerly the Standard Oil Company (New Jersey).

An analysis of the rents associated with Norman Wells crude oil production between the beginning of 1970 and the end of 1974 revealed the following:

1. The present value in 1975 of these past rents amounted to $32.4 million if taxes are excluded, and to $34.5 million if taxes are included.

2. Of the tax-exclusive total, consumers of Norman Wells products received $25.4 million, or 78.4 per cent, Imperial Oil received $3.7 million, or 11.3 per cent, and the federal government received $3.3 million, or 10.3 per cent.

3. Of the tax-inclusive total, consumers received $25.4 million, or 73.6 per cent, the federal government received $5.4

million, or 15.8 per cent, and Imperial Oil received $3.7 million, or 10.6 per cent.

The reasons for this structure of rent distribution relate to both the federal government/Imperial Oil financial relationships that characterize Imperial's operation at Norman Wells, and to federal government local and national pricing policies. With respect to the former, the revenue-sharing arrangement negotiated between the federal government and Imperial Oil regarding Norman Wells crude oil production results in the federal government receiving (a) one third of the net value of natural gas and crude oil production, plus (b) a 5 per cent royalty on the gross value of the remaining two thirds, minus (c) an Imperial Oil management fee calculated as 10 per cent of the federal government's share of production and development costs. In return, Imperial Oil is allowed to expense all development expenditures as they occur, instead of having to apply the standard write-off procedures.

Secondly, the federal government apparently regulates the prices of Norman Wells refined products in such a way that the value of crude oil production is undervalued relative to the Alberta wellhead price plus transportation costs. For example, in 1974 Norman Wells crude oil was valued at $3.32/barrel, whereas the Western Canada average was $5.72/barrel. If transportation costs were $1/barrel, Norman Wells crude oil was undervalued in 1974 by $3.40/barrel.

In addition to this, federal government policy with respect to the pricing of Canadian crude oil in general results in an undervaluation of the Alberta wellhead price relative to the world oil price. In 1974 the world oil price was around $11/barrel

The Western Canada average was, as we have seen, $5.72/barrel, resulting in an undervaluation of the Alberta wellhead price relative to the world price of $5.28/barrel. Adding this to the undervaluation previously derived results in an undervaluation of Norman Wells crude oil in 1974 of $8.68/barrel.

Although the information currently available does not allow an exact identification of the consumer rent recipients, some indication of these entities is possible. In 1974 the anticipated sales value of refined products at Norman Wells was estimated at just over $6 million. Of this total diesel fuel oil accounted for 41.3 per cent and aviation turbo fuel for 33 per cent. It would therefore seem that the major share of the rents associated with Norman Wells crude oil production accrue to the corporate sector.

Mining

Between 1970 and 1974 six mining projects were operative in the Northwest Territories. The Pine Point and Con/Rycon mines are both majority-owned and controlled by Cominco, which is in turn majority-owned and controlled by Canadian Pacific Investments Ltd. The Giant Yellowknife mine is 19 per cent owned by Falconbridge Nickel Mines. The Canada Tungsten mine is 42 per cent owned by American Metal Climax Incorporated. The Echo Bay mine is owned by the International Utilities Corporation of Philadelphia.

An analysis of the rents associated with the activities of these mines between the beginning of 1970 and the end of 1974 revealed the following:

1. The present value in 1975 of these past rents amounted to $117.6 million if taxes are excluded, and to $195 million if taxes are included.

2. Of the tax-exclusive total the mining companies retained $102.5 million, or 87.1 per cent, in the form of excess profits, while the federal government received $15.1 million, or 12.9 per cent from royalties.

3. Of the tax-inclusive total, the companies retained $102.5 million, at 52.6 per cent, in the form of excess profits, while the federal government received $77.4 million, or 39.6 per cent, from taxes, and $15.1 million, or 7.8 per cent from royalties.

This structure of rent distribution is basically the result of federal government royalty and taxation policies as they apply to natural resources projects in the Northwest Territories. Within this institutional structure, the companies are seen to retain over 85 per cent of the tax-exclusive rents in the form of excess profits because of the rather generous royalty arrangements that are operative. In the southern provinces, by contrast, a much smaller share of tax-exclusive rents would accrue to the companies, because provincial mining taxes and royalty arrangements would appropriate a greater share for the benefit of the people.

The rents retained by the companies are presumably either paid out in the form of dividends to shareholders, or are used to finance investments which enhance the long-term viability and profitability of corporate operations. The location of these investments may be in Canada, the United States, or in any country in which the ultimate rent recipients perceive their long-term interests to lie.

Consider the activities of Cominco, which owns 69 per cent of the Pine Point mine, 100 per cent of the Con mine and 76 per cent of the Rycon mine. During the 1970-1974 period these mines

between them received $75.3 million in rents from their activities in the Northwest Territories. This represents 73.5 per cent of all company-retained rents associated with mining projects in the Northwest Territories during these years. On the basis of its ownership interests in these mines the bulk of these rents would have accrued to Cominco. A portion of these rents may have been retained at the mines, another portion paid out to Cominco's shareholders (of which Canadian Pacific Investments Ltd. would have received 54 per cent), and the rest used to help finance investments contributing to the long-term viability and profitability of the corporation.

During the 1970-1974 period, for example, Cominco was engaged in reopening the H.B. lead and zinc mine near Salmo in British Columbia, in opening the Black Angel mine in western Greenland, in gaining an Australian base of operations by acquiring a 55 per cent interest in Aberfoyle Ltd., and in rehabilitating the Vade potash mine in Saskatchewan. At the present time Cominco is engaged in constructing a new ammonia-urea complex near Carseland, Alberta, at an estimated cost of $130 million. Its current exploration projects are concerned with diamonds in the Central African Republic, copper-molybdenum in Mexico, zinc in Kentucky, oil and gas in Texas and New Mexico, lead-zinc-copper-silver in Tasmania, and, somewhat closer to home, lead-zinc and uranium in the Northwest Territories.

While these activities reveal sound corporate long-term strategy, they quite obviously have little to do with the development problems of the native peoples in the Northwest Territories. At the same time as the economic rents associated

with Cominco's current mining projects in the Northwest Territories contribute to the viability and profitability of its long-term operations, they fail to contribute in any meaningful way to the long-term development objectives of the native peoples. The reason is quite straight forward. The institutional arrangements governing natural resources projects in the Northwest Territories provide no mechanism by which the native peoples can obtain a share of the economic rents associated with their activities.

## THE IMPLICATIONS

The implications that follow from this evidence may be stated as follows:

1. The institutional arrangements governing natural resources projects in the Northwest Territories result in the economic rents associated with their activities failing to contribute to the long-term development objectives of the native peoples.

2. If such natural resources projects, and those envisaged in the future, are to contribute to native peoples development, the institutional arrangements governing their activities must be changed in a fundamental way.

3. The native peoples do not appear to be able to rely on the federal government to adequately represent their interests in this endeavour.

This third implication arises from a consideration of some further aspects of the Pointed Mountain gas project. In his Introductory Remarks before the House of Commons Standing Committee on Indian Affairs and Northern Development in March 1972, prior to the statement of the Governments Northern Objectives Priorities and

Strategies for the 70's, the then Minister of Indian Affairs and Northern Development, the Honourable Jean Chrétien, stated:

> Fundamental to the Government's statement is our belief that native northerners should derive early, visible, and lasting benefits from economic development. Our efforts must not only be turned to developing the natural resources of the North for the benefit of Canada as a whole. The development of northern resources must first improve the standard of living and the well-being of northern residents. All too often the economic activity of the past was at their expense (39).

This statement was made in March, 1972, when construction relating to the Pointed Mountain project was already underway. But Edgar Dosman, in his recently published book The National Interest indicates that this policy statement had been approved by the Cabinet in July, 1971 (40), prior to any significant construction activity. Further, a report submitted to Westcoast Transmission by Shultz International Limited, entitled Ecological and Economical Impact of the Pointed Mountain Natural Gas Line, and available to the federal government by September, 1971, had already assessed the likely distribution of the economic benefits associated with the project. After noting that benefits during the construction phase in terms of equipment purchases and personnel requirements would accrue to British Columbia, Alberta, and other southern provinces receiving the appropriate contracts, the report went on to analyze the longer-term benefits in the following way:

> Generally, the benefits of the proposed pipeline will be to the nation as a whole, as a result of the export of gas to the United States and the corresponding foreign exchange inflow which will result. The national economy will also benefit to the extent that Westcoast's profits will be distributed to Canadian shareholders.....

> Further, the net value of economic activity generated, both directly, and indirectly through the multiplier, will benefit Canada as a whole [53].

We have, then, a situation where, on the one hand, the Cabinet has approved a policy statement in which it is emphasized that natural resources projects should not only benefit Canada as a whole, but instead should result in "early, visible, and lasting benefits" to the native peoples, and on the other hand an evaluation stating that the Pointed Mountain project will do precisely the opposite. One would naturally conclude that under these circumstances the federal government would not approve the project unless or until it had altered the institutional arrangements governing the project so that the native peoples would benefit. In fact, exactly the contrary occurred. The federal government approved the Pointed Mountain project by granting a right-of-way to Westcoast Transmission in November, 1971. It then released its public policy statement to the House Standing Committee in March, 1972, with construction well underway. The institutional arrangements governing the project then resulted in U.S. corporate and/or consumer interests receiving over 75 per cent of the economic rents associated with the project by the end of 1974, with Canadian entities in British Columbia receiving most of the rest.

The conclusion that must be drawn from any objective consideration of this evidence is clear. The native peoples cannot rely on the federal government alone to represent their interests in the case of proposed natural resources projects in the Northwest Territories. A more fundamental change in the institutional arrangements governing these projects is required.

## CONCLUSION

The institutional arrangements governing natural resources projects in the Northwest Territories result in the economic rents, and hence the long-term benefits, from their activities accruing to U.S. producers and consumers, to Canadian entities in British Columbia, to the Canadian corporate sector, to U.S. and Canadian corporate investors, and to the federal government. The native peoples of the Northwest Territories, faced with serious development problems, receive none.

The proposed Mackenzie Valley natural gas pipline, operating within the same institutional structure, will produce similar results. If this is not to occur, fundamental changes in the institutional arrangements governing natural resources projects in the Northwest Territories must first be implemented, because the federal government has proved itself unable or unwilling to represent the interests of the native peoples.

The position of the native peoples is that there should be no pipeline before a negotiated land claims settlement. Whatever the other merits of this position, the evidence presented here indicates it makes sound economic sense.

# APPENDIX A
# WITNESS RESUME

# CURRICULUM VITAE

## PERSONAL INFORMATION

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## EDUCATION

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|---|---|
| 1969 | B. Sc. (ECON), University of Hull, England. |
| 1971 | M.A. (ECONOMICS), University of Guelph. |
| 1974 | All Ph. D. course and residence requirements completed in the Department of Political Economy at the University of Toronto. |

## EXPERIENCE

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|---|---|
| 1969-70 | Systems Analyst, National Data Processing Service, London, England. |
| 1971-72 | Research Assistant, Department of Economics, University of Guelph, Ontario |
| 1974-75 | Economic Research Analyst, Indian Brotherhood of the Northwest Territories, Yellowknife, N.W.T. |

# APPENDIX B

List of reports etc referred to or relied on

# REFERENCES


(1) Science Council of Canada, Discussion Paper on Nothern Development (Ottawa: Science Council of Canada, 1975), p. 46.

(2) National Energy Board, Report to the Governor in Council In the Matter of the Pricing of Natural Gas Being Exported under Existing Licences (Ottawa: National Energy Board, 1974), p. 6-A.

(3) The Honourable Jean Chretien, A Report to the Standing Committee on Indian Affairs and Northern Development on the Government's Northern Objectives, Priorities and Strategies for the 70's - Introductory Remarks in Science and the North (Ottawa: Information Canada, 1973), p. 273.

(4) Edgar J. Dosman, The National Interest (Toronto: McClelland and Stewart, 1975), p. 99.

(5) Shultz International Limited, Ecological and Economical Impact of the Pointed Mountain Natural Gas Line (Vancouver: Schultz International Limited, 1971), p. V/21.